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U.S. ANTITRUST AGENCIES TAKE AIM AT PRIVATE EQUITY

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The FTC's recent settlements in two separate acquisitions by JAB Consumer Partners SCA SICAR ("JAB") were—with one notable exception—unremarkable. In the first settlement, in June 2022, JAB, a $55 billion private equity fund, agreed to divest six veterinary clinics in Austin, Texas; San Francisco, California; and the East Bay area (Oakland, Berkeley, and Concord, California) to resolve the Federal Trade Commission's ("FTC")[1] concerns that JAB's $1.25 billion acquisition of SAGE Veterinary Partners, LLC ("SAGE") reduced competition in those markets. In the second deal, later in June, JAB agreed to divest five veterinary clinics in and around Richmond, Virginia; Washington, D.C.; Denver, Colorado; and San Francisco, California to address the FTC's concerns that JAB's $1.65 billion acquisition of VIPW, LLC and Ethos Veterinary Health LLC ("Ethos") reduced competition in those markets. The Commission's five commissioners, now with a three-to-two Democratic majority, unanimously voted to accept the FTC's complaint and settlement in each matter.

Taking the FTC's complaints at face value, JAB's acquisitions in the markets described above would have resulted in high market shares and concentration, left few remaining competitors, and/or combined veterinary providers that were particularly close competitors. For example, the FTC alleged that JAB's acquisition of SAGE would have resulted in a monopoly in the provision of neurology and ophthalmology veterinary services in San Francisco and its acquisition of Ethos would have resulted in a monopoly in medical oncology veterinary services in Richmond. The full Commission (all five commissioners) agreed on these points.

But that's where the harmony ended. The Commission divided along party lines concerning whether to impose "prior approval" and "prior notice" requirements in the FTC's settlements with JAB, as well as a key reason for those obligations, which turned on

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JAB's purported "buy-and-buy" private equity business model.

For some context, in a controversial move in October 2021, the Commission voted to revive a long-abandoned policy that Commission orders settling FTC merger investigations include a "prior approval" clause that grants the FTC the unilateral authority to approve (or deny) certain future transactions for a minimum of 10 years.[2] At the time, the FTC warned that it may seek prior approval for future transactions involving product or geographic markets beyond the scope of the markets in which the FTC alleges harm from the initial transaction. Since the October 2021 policy change, the FTC has imposed prior approval in *all* of its settlements with merging parties. With limited exceptions, however, prior approvals have not extended far beyond the product or geographic markets in which the FTC alleged harm to competition.[3]

In the two JAB settlements, the Commission required "out-of-market" prior approval and prior notice clauses, described by the FTC Chair Lina Khan as "the first of its kind in a Commission order:"

- ***Prior Approval***: If JAB seeks to buy a veterinary clinic located within 25 miles of any JAB clinic anywhere in California, Colorado, Maryland, Texas, Virginia, or the District of Columbia any time during the next 10 years, JAB must seek the FTC's affirmative approval for the purchase. This requirement extends beyond the handful of local metro markets identified in the complaint.
- ***Prior Notice***: JAB must provide the FTC with 30-day advance written notice before JAB attempts to acquire a veterinary clinic within 25 miles of a JAB clinic anywhere in the United States that JAB owns now or in the future.

The FTC Chair, joined by the other two Democratic commissioners, commented that the "extra protections" were warranted for two reasons: (i) to stall the "rapid pace" of JAB's consolidation of veterinary clinics, and (ii) because JAB had previously entered into a consent order with the Commission in February 2020 related to its $5 billion acquisition of MedVet Associates, LLC, which resulted in a consent order with the FTC in which the parties agreed to divest three veterinary facilities in South Carolina, New York/Connecticut, and Northern Virginia.

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In a statement issued in connection with the SAGE acquisition, the FTC majority criticized "serial acquisitions or 'buy-and-buy' tactics [] used by private equity firms and other corporations to roll up sectors, enabling them to accrue market power and reduce incentives to compete, potentially leading to increased prices and degraded quality."[4] The majority also criticized "private equity firms' playbook for purchasing or investing in companies" which "can include tactics such as leveraged buyouts, which saddle businesses with debt and shift the burden of financial risk in ways that can undermine long-term health and competitive viability."[5] Although the majority acknowledged that private equity firms "can support expansion and upgrades," "firms that seek to strip and flip assets over a relatively short period of time are focused on increasing margins over the short-term, which can incentivize unfair or deceptive practices and the hollowing of productive capacity."[6] The majority, however, did not allege that JAB had any plan to "strip and flip" any of the veterinary clinics it acquired, or that it had done so following its previous acquisitions. The majority even went as far as to say that "[r]esearch has shown that private equity ownership of elder care facilities is correlated with increased deaths at those nursing homes, potentially owing to cost-cutting measures like staff reductions."[7]

The two Republican commissioners issued a concurring statement in the SAGE transaction, objecting "to the Complaint's invocation of rhetoric unrelated to competition and the order's apparent predication of remedies upon both that rhetoric and the majority's evident distaste for private equity as a business model, instead of the facts uncovered in the investigation."[8] According to the minority, the evidence showed competitive harm in just three local markets in the SAGE transaction (Austin, San Francisco, and the East Bay), and the majority's allegation about a "growing trend" of consolidation in veterinary clinics did not justify the broad prior approval and prior notice obligations. The minority commented that consolidation on a national level was "irrelevant" and "untethered to any impact on competition," because "there [was] no national market for emergency and specialty veterinary services." In addition, the minority observed that even if there were such a market, JAB would have fewer than 100 clinics nationwide, holding a "competitively meaningless share of the purported national market." The minority also expressed concern about the majority's comment that additional remedies were justified because JAB is a private equity firm: "Imposing heightened legal obligations on disfavored groups—including private equity—because of who they *are* rather than what they have *done* raises rule of law concerns."

Skepticism of Private Equity Is Not New at the Antitrust Agencies

For a number of years, some at both antitrust agencies expressed skepticism about the commitment of private equity buyers to operate divestiture assets for the long-term.[9] That view—even if ill-informed—led divestiture sellers to look past private equity in divestiture transactions. In addition, during the Trump administration, FTC Commissioner Rohit Chopra, now Director of the Consumer Financial Protection Bureau, also took a tough stance against private equity transactions. The FTC's current Chair worked for Commissioner Chopra at the FTC and her public statements invoke some of the same language in former Commissioner Chopra's statements.

In a dissenting statement in the FTC's settlement over Staples' acquisition of Essendant, then-Commissioner Chopra expressed concern that Sycamore Partners, the private equity firm that controlled Staples, had an "investment approach and track record [that] suggest that the fund will operate assets

much differently than a typical buyer, in ways that lead to higher margins, without any guarantee of greater output and service offerings."[10] Commissioner Chopra complained that the FTC "failed to consider Sycamore's incentives," noting that the FTC approved Sycamore as a divestiture buyer in a dollar store merger, but that Sycamore "quickly resold the assets." On Twitter, Chopra asked "Do you think we should let a private equity fund and Staples have more power over what we buy and how much we pay for office supplies?"[11]

More broadly, Chopra encouraged the FTC to "closely scrutinize any HSR filings by private equity firms to gain insight on their future acquisitions that may be non-reportable."[12] Chopra claimed that private equity firms "quietly increase market power and reduce competition" through a "build-and-buy" strategy involving an "initial takeover of a platform company with subsequent 'bolt-on' and 'tuck-in' acquisitions." Chopra further alleged that many of those transactions were below the HSR reporting threshold, and encouraged the FTC to make changes to "help the agency detect harmful roll-up activity."[13]

In a pair of interviews given to the *Financial Times* in late May and early June of this year, the leadership of both the U.S. Department of Justice Antitrust Division ("DOJ") and FTC were critical of private equity transactions. The DOJ official warned that "sometimes" a private equity firm plans to "hollow out or roll up an industry and essentially cash out,"[14] stating that the "business model is often very much at odds with the law and very much at odds with the competition we're trying to protect."[15] Weeks later, in an interview also with the *Financial Times*, FTC leadership warned that it was "skeptical" of private equity transactions, previewing its comments about the JAB/SAGE settlement just a few weeks later.[16]

Key Takeaways & Looking Ahead

Below we summarize what private equity should expect from antitrust reviews in the current environment in light of the developments detailed above, and describe what might be next from the U.S. antitrust authorities.

1. What once was heated rhetoric about private equity has now resulted in enforcement actions, at least at the FTC. The JAB settlement confirms that the antitrust agencies are doing more than just "talking tough."

2. Notwithstanding the first takeaway, the antitrust substance matters. The DOJ and the FTC receive HSR filings in hundreds of private equity transactions each year. In the large majority of those transactions, no investigation is necessary because there is no horizontal overlap or vertical connection that merits further inquiry. Taking the FTC's complaints at face value, the FTC grounded the need for a remedy in traditional antitrust concerns and theories of harm, the Commission voted unanimously on the need for a remedy, and both JAB transactions ultimately proceeded with limited divestitures. Although the majority's negative views about private equity appear to have led to the broad prior approval and prior notice clauses, the majority did not attempt to block either transaction outright. If the FTC attempted to stretch beyond a cognizable antitrust theory, it would likely face an uphill battle in the courts where decades of case precedent still matters.

3. Private equity buyers should weigh the risk of a broad prior approval or notice clause if a transaction involves a risk of an FTC divestiture, which should be a risk only in a small number of transactions. If a broad prior approval clause is unpalatable to the buyer, then

the only solution might be to "litigate the fix." In that strategy, the parties sign a contingent divestiture agreement with a divestiture buyer and argue to a court (following the FTC investigation and filing of a complaint) that their prepackaged remedy solves the FTC's concerns.

4. Private equity buyers should evaluate how to sequence their M&A pipeline. For example, a buyer might consider whether to pursue a strategically important acquisition without traditional antitrust concerns prior to another transaction that may be less important but carries the risk of a prior approval or notice clause.

5. The DOJ and the FTC are revising their merger guidelines. The guidelines outline the types of competitive issues that can result from deals between competitors (horizontal) and between companies operating at different levels of the supply chain (vertical), and describe how the agencies will evaluate those issues. Over the past two decades, most judges have embraced the horizontal merger guidelines as the proper analytical framework for evaluating mergers that the agencies challenge in court. Although the guidelines historically have not had special rules for private equity M&A, it would not be surprising if the new guidelines call for scrutiny of "roll-up" or "serial" acquisitions, as well as scrutiny of the "incentives" of private equity firms. Unless those guidelines are based on widely accepted and sound antitrust theories, however, they are less likely to receive the same broad adoption as past iterations, including from the courts, and may not survive the next administration.

6. In September 2020, the FTC announced proposed rulemaking that could increase the number of private equity acquisitions that must be notified to the FTC and the volume of information that private equity firms must provide about "associates" in connection with those filings. The FTC is likely to adopt those changes in the coming years.

The views and opinions set forth herein are the personal views or opinions of the authors; they do not necessarily reflect views or opinions of the law firm with which they are associated.

ENDNOTES:

[1]We use the term "FTC" to refer to the agency or staff investigating the transactions, but the term "Commission" to distinguish the FTC's five commissioners.

[2]*See* Michael Gleason, Lin Kahn, J. Bruce McDonald, Jeremy Morrison, and Craig Waldman, FTC Resurrects Unilateral Preapproval in Merger Investigation Settlements to Halt Future "Anticompetitive" M&A (Nov. 2021), https://tinyurl.com/5n7nvzma.

[3]For example, in the FTC's settlement with DaVita, Inc. related to its proposed acquisition of Total Renal Care, the FTC defined the relevant geographic market to include the "greater Provo, Utah area," but adopted a prior approval clause that extends to the entire state of Utah.

[4]*In the Matter of JAB Consumer Fund/SAGE Veterinary Partners*, No. 2110140, at 3 (June 13, 2022) (Statement of Chair Lina M. Khan, Joined by Commissioner Rebecca Kelly Slaughter and Commissioner Alvaro M. Bedoya), https://www.ftc.gov/system/files/ftc_gov/pdf/2022.06.13 - Statement of Chair Lina M. Khan Regarding NVA-Sage - new.pdf.

[5]*Id.*

[6]*Id.*

[7]*Id.* Citing a *Buzzfeed News* article, the Commission majority even went as far as to suggest that private equity-owned group homes have led to "failed inspections, overworked staff, and even deaths." *Id.*

[8]*In the Matter of JAB Consumer Fund/SAGE*

Veterinary Partners, No. 2110140, at 1 (June 13, 2022) (Concurring Statement of Commissioners Noah Joshua Phillips and Christine S. Wilson), https://www.ftc.gov/system/files/ftc_gov/pdf/2110140C4766NVASAGEPhillipsWilsonConcurringStatement.pdf

[9]*See* Makan Delrahim, Assistant Attorney General, U.S. Dep't of Justice, Antitrust Division, Remarks at Georgetown Law's Global Antitrust Enforcement Symposium (Oct. 6, 2020), https://www.justice.gov/opa/speech/assistant-attorney-general-makan-delrahim-delivers-remarks-georgetown-laws-global. Late in the Trump administration, the DOJ issued new remedies guidelines that for the first time addressed the treatment of private equity in forced DOJ divestiture remedies, upending the DOJ's assumptions about private equity buyers in DOJ remedies. The DOJ observed that private equity held onto investments for longer periods, invested in the businesses it purchased, and added expertise to management teams. The DOJ also cited the FTC's January 2017 merger remedies study for the proposition that in some cases, private equity offered a flexible investment strategy, and was willing to invest more into the divestiture business when necessary.

[10]*In the Matter of Sycamore Partners II, L.P., Staples, Inc., and Essendant Inc.*, No. 181-0180, at 4 (Jan. 18, 2019), (Dissenting Statement of Commissioner Rohit Chopra), https://www.ftc.gov/system/files/documents/public_statements/1448335/181_0180_staples_essendant_chopra_statement_1-28-19_0.pdf.

[11]Rohit Chopra (@chopracfpb), Twitter (Jan. 28, 2019, 6:05 PM), https://twitter.com/chopracfpb/status/1090023141303300097.

[12] *Statement of Commissioner Rohit Chopra Regarding Private Equity Roll-ups and the Hart-Scott Rodino [sic] Annual Report to Congress*, File No. P110014, at 2 (July 8, 2020), https://www.ftc.gov/system/files/documents/public_statements/1577783/p110014hsrannualreportchoprastatement.pdf.

[13]Citing his own letter to Congress, Chopra further alleged that in health care, private equity has led to "other collateral consequences," including "the scourge of surprise medical billing by out-of-network physicians and 'body brokering' in the treatment of opioid dependency." *Id.*

[14]Stefania Palma and James Fontanella-Khan, *Crackdown on buyout deals coming, warns top U.S. antitrust enforcer*, Financial Times, May 19, 2022, https://www.ft.com/content/7f4cc882-1444-4ea3-8a31-c382364aace1.

[15]*Id.*

[16]Stefania Palma, Mark Vandevelde, James Fontanella-Khan, *Lina Khan vows 'muscular' U.S. antitrust approach on private equity deals*, Financial Times, June 9, 2022, https://www.ft.com/content/ef9e4ce8-ab9a-45b3-ad91-7877f0e1c797.

DELAWARE SUPREME COURT REVERSES DISMISSAL OF A POST-MERGER SUIT FOR ALLEGED BREACH OF FIDUCIARY DUTY RELATED TO DISCLOSURES ON APPRAISAL RIGHTS

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On July 19, 2022, in an opinion authored by Justice Gary F. Traynor in *In re GGP, Inc. Stockholder Litigation*,[1] a majority of the Supreme Court of Delaware sitting *en banc* affirmed in part and reversed in part the dismissal of breach of fiduciary duty claims against the directors of a real estate investment trust (the "Company") asserted by former stockholders of the Company after its acquisition. Plaintiffs alleged that the merger was structured to eliminate the statutory appraisal rights of the Company's stockholders and that the proxy